Supreme Court, U.S.
FILED
SEP 13 1985
JOSEPH F. SPANIOL, JR.
CLERK

No. 84-1737

IN THE
Supreme Court of the United States
OCTOBER TERM

UNITED STATES OF AMERICA,
Petitioner,

v.

AMERICAN COLLEGE OF PHYSICIANS,
Respondent.

ON A PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

BRIEF FOR AMERICAN BUSINESS PRESS AS AMICUS CURIAE IN SUPPORT OF THE BRIEF OF THE UNITED STATES

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BRIEF FOR AMERICAN BUSINESS PRESS AS AMICUS CURIAE IN SUPPORT OF THE BRIEF OF THE UNITED STATES

QUESTION PRESENTED

Is the Unrelated Business Income Tax enacted into law in 1950, as amplified in the Tax Reform Act of 1969 which specifically declared that tax applicable to advertising profits earned from the sale of advertising in periodicals published by tax-exempt organizations, to be invalidated because of an erroneous decision of the United States Court of Appeals for the Federal Circuit holding those advertising profits non-taxable.

INTEREST OF AMICUS CURIAE AMERICAN BUSINESS PRESS

On June 5, 1985 American Business Press (ABP)[1] filed a motion to file an amicus curiae brief in support of the Petition of the United States for a Writ of Certiorari to review the judgment of the United States Court of Appeals for the Federal Circuit in *American College of Physicians* v. *United States*, 743 F.2d 1570 (1984). Pursuant to Sup. Ct. R. 36.1, ABP's amicus brief accompanied its June 5 motion. On July 1, 1985 this Court entered an order granting ABP's motion, and simultaneously granted the Government's petition for a writ of certiorari. The Solicitor General and Counsel for respondent American College of Physicians (ACP) have consented to ABP's request that it file an amicus curiae brief pursuant to Sup. Ct. R. 36.2.

ABP is the nation's association of leading trade journal publications. Over 500 scientific, professional, educational and other types of specialized periodicals circulated within the United States and throughout the world are published by ABP's members. As this brief and ABP's brief in support of the petition for certiorari show, ABP members in a wide variety of fields edit publications which are in direct competition with periodicals issued by tax-exempt organizations classified as either 26 U.S.C. §501(c)(3) or 26 U.S.C. §501(c)(6) entities. The types of advertising appearing in ABP periodicals and in §501(c)(3) and § 501(c)(6) periodicals are identical.

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[1]On July 1, 1985 the name of the association was changed to Association of Business Publishers. In the interest of continuity, the name American Business Press is used in this brief. The initials "ABP" mean either American Business Press or Association of Business Publishers.

SUMMARY OF ARGUMENT

The common threads of unfair competition and closure of tax-loopholes run through the administrative, legislative and judicial histories of the Unrelated Business Income Tax (UBIT) from the date it was passed by Congress in 1950. Pub. L. No. 81-814, §301, 64 Stat. 906, (1950) (codified at 26 U.S.C. §§511-513). The 1967 Treasury regulations[2] issued pursuant to UBIT specifically applied UBIT to the advertising profits of *all* tax-exempt organizations. The Treasury regulations contain seven examples of exploitation of an exempt function. Appendix A hereto contains Treasury Regulation §1.513-1(d)(4)(iv) headed "Exploitation of exempt functions", which pertains to advertising, and Examples 6 and 7 thereunder, both particularly relevant to the instant case.

Examples 6 and 7 illustrate how the advertising carried in a periodical published by a business league (§501(c)(6) organization) or in a periodical published by a professional society (§501(c)(3) organization) is exploitation[3] of that exempt function. Example 7 issued in *1967* describes respondent ACP's exploitation of *its* exempt function in *1985* precisely.

In the case of a periodical which contains both editorial and advertising content, whether the tax classification of the exempt organization be §501(c)(3) or §501(c)(6), both the Treasury regulations and Congress declared advertising to be unrelated to any tax-exempt purpose and there-

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[2]Treas. Reg. § 1.513-1(d) (1967).

[3]By way of illustration, if the publishing of editorial content in a tax-exempt organization's periodical is a related, tax-exempt function, then the sale of advertising in that periodical is exploitation of an exempt function (editorial content) and the profits earned on that advertising are taxable.

fore taxable. Congress further directed IRS to prescribe accounting regulations "so as to clearly reflect unrelated business taxable income from such activity and to prevent avoidance of unrelated business income tax liability." H.R. Rep. No. 91-413, 91st Cong., 1st Sess., *reprinted in U.S. Code Cong. & Ad. News* 1696 (1969). The accounting regulations (Treasury Regulation §1.512(a)-1 *et seq.*) took effect December 18, 1975. 40 Fed. Reg. 58638.

ARGUMENT

I. IN ADDITION TO TAX COLLECTION THE PRIMARY PURPOSE OF UBIT IS TO PREVENT UNFAIR COMPETITION

Since 1950, the courts of appeal have uniformly emphasized the UBIT purpose of preventing unfair competition. The Fifth Circuit in *Louisiana Credit Union League* v. *United States,* 693 F.2d 525, 539 (5th Cir. 1982) held:

> A fair reading of the legislative history of the Revenue Act of 1950 indicates that Congress indeed was concerned that exempt institutions choosing to enter the marketplace would enjoy an unfair advantage over their taxpaying competitors. See H.R. Rep. No. 2319, 81st Cong., 2d Sess., reprinted in 1950-2 C.B. 380; S. Rep. No. 2375, 81st Cong., 2d Sess., reprinted in 1950-2 C.B. 483; 96 Cong. Rec. 9351, 9366 (1950) (statement of Mr. Lynch). *Congress reiterated its interest in preventing unfair competition when section 513 was amended in 1969.* Similar language accompanied further amendments in 1978. [Footnotes omitted and emphasis supplied][4]

[4]The *1969* amendment to UBIT enacted in 1950, as referred to in *Louisiana Credit Union,* was enacted primarily to deal with advertising in tax-exempt periodicals, particularly in medical journals. This is the Congressional enactment before the Court in the case at bar. The *1978*

In *Hope School* v. *United States,* 612 F.2d 298, 304 (7th Cir. 1980), the Court of Appeals said that unfair competition is "the primary consideration" when a court determines whether a tax-exempt organization is conducting an unrelated trade or business.

The Second and the Sixth Circuits, like the Fifth and Seventh Circuits, have also declared that the purpose of Congress in extending the income tax to the unrelated business income of tax-exempt organizations was to eliminate the unfair competitive advantage over taxpayers that tax-exempt organizations like respondent enjoy when they engage in an unrelated trade or business. *Rensselaer Polytechnic Institute* v. *Commissioner,* 732 F.2d 1058, 1061 (2d Cir. 1984); *Service Bolt & Nut Co.* v. *Commissioner,* 724 F.2d 519, 524 (6th Cir. 1983).

As recently as June 14, 1985, in *American Medical Association* v. *United States,* a case also involving the applicability of UBIT to medical advertising profits, Judge Grady of the United States District Court, Northern District of Illinois, re-affirmed this purpose of UBIT when he wrote:

> It could be argued that a tax law is exclusively a matter of government interest, since its basic purpose is to generate revenue. But case law indicates that the purpose of the tax law and regu-

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amendment referred to by the Court exempted bingo games conducted by tax-exempt organizations and political organizations if those games do not compete with bingo games carried on by for-profit businesses. The 1978 Ways and Means Committee Report referred to by the Court states:

> In general, the unrelated business income tax was imposed to prevent tax-exempt organizations from having an unfair competitive advantage over taxable businesses. . . .

H.R. Rep. No. 95-1608, 95th Cong., 2d Sess., *reprinted in U.S. Code Cong. & Ad. News* 3718 (1978).

> lations here in question is to maintain fair competition between tax-exempt and non-tax-exempt businesses. *See* Rensselaer Polytechnic Institute v. Commissioner of Internal Revenue, 732 F.2d 1058, 1061 (2d Cir. 1984); Louisiana Credit Union League v. United States, 693 F.2d 525, 539 (5th Cir. 1982). Therefore public interest issues similar to those found in antitrust cases appear to be at stake here.

No. 82-C-7213, mem. op. at 11, n.5 (N.D. Ill. 1985).

Congress had ample opportunity in 1978-1981 to reverse its specific position declaring advertising profits of tax-exempt organizations taxable, but did not do so. Congressman Conable introduced H.R. 13740 in the 95th Congress and H.R. 990 in the 96th and 97th Congresses: These bills would have gutted the tax on advertising profits of tax-exempt organizations. No hearings were ever held on them, and no similar bill was introduced in the 98th Congress. Thus the intent of Congress that advertising is an unrelated business activity remains intact to the very date of this brief.

Legislative and judicial precedent notwithstanding, the Federal Circuit utterly disregarded (1) unfair competition, (2) Treasury Regulation § 1.513-1(d)(4)(iv), (3) Example 7 thereunder, and (4) Congressional intent when that Court declared respondent's advertising profits tax-exempt, even though that advertising is identical to that carried by its taxpaying competitors.[5]

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[5]The will of Congress to the contrary, the Federal Circuit erroneously criticized Chief Claims Court Judge Kozinski's decision to apply UBIT to ACP's advertising profits, in stating:

> The trial court's analysis places too great an emphasis on the similarity of the activity to commercial advertising.

American College of Physicians v. United States, 743 F.2d 1570, 1576 (1984).

II. WHEN CONGRESS PASSED UBIT IN 1950 IT MADE IT POSSIBLE FOR A TAX-EXEMPT ORGANIZATION WHICH OPERATED A BUSINESS TO KEEP ITS EXEMPTION

A tax-exempt organization, whether §501(c)(3) or §501(c)(6), must meet three tests established by law and regulations:[6]

1. The *exclusivity* test: A tax-exempt organization must be organized exclusively for the tax-exempt purposes set forth in its charter, or risk loss of its tax-exempt status. Treasury Reg. §1.501(c)(3)-1(c). *Better Business Bureau* v. *United States,* 326 U.S. 279, 282 (1945); *P.L.L. Scholarship Fund* v. *Commissioner,* 82 T.C. 197, 199 (1984).

2. The *incidental but not substantial* test: Where substantial commercial income is mixed with incidental income related to a tax-exempt purpose, tax-exemption can be lost. Treasury Reg. §1.501(c)(3)-1(e). *Scripture Press Foundation* v. *United States,* 285 F.2d 800, 803 (Ct. Cl. 1961), cert. denied, 368 U.S. 985 (1962); *B.S.W. Group, Inc.* v. *Commissioner,* 70 T.C. 352, 357-358 (1978).

3. The *no benefit inuring* test: No part of net earnings of a nonprofit organization can inure to the benefit of any private shareholder or individual without risking loss of tax-exemption. Treas. Reg. §1.501(c)(3)-1(c). *Founding Church of Scientology* v. *United States,* 412 F.2d 1197, 1199 (Ct. Cl. 1969), cert. denied, 397 U.S. 1009 (1970); *Unitary Mission Church* v. *Commissioner,* 74 T.C. 507, 513 (1980).

When Congress passed the UBIT, it made it possible for a tax-exempt business to keep its tax exemption by making any unrelated business conducted by that organization taxable. Without UBIT, many organizations, including

[6]26 U.S.C. § 501(c); Treas. Reg. §1.501(c).

professional societies like respondent ACP, could be subject to loss of tax exemption because they would not qualify under the foregoing tests.

Thus, if UBIT did *not* apply to the advertising profits of respondent, ACP could lose its tax exemption because a benefit inures to the individual doctors who are the members and thus the owners of ACP. This inurement can take a variety of forms, including lower dues made possible by using advertising profits to finance ACP's activities. The same situation applies to the activities of all other tax-exempt organizations.

Prior to passage of UBIT, untaxed profits earned from advertising could be used to educate doctors or for any other worthwhile purpose because the test prior to 1950 was the *destination* of income earned by commercial activities, and not the *source* of the income. *See Roche's Beach, Inc.* v. *Commissioner,* 96 F.2d 776, 778 (2d Cir. 1938).

One of the situations which brought about passage of UBIT was ownership by New York University of C.F. Mueller Company, a pasta company. *See C.F. Mueller Co.* v. *Commissioner,* 190 F.2d 120 (3d Cir. 1951). While New York University channeled its macaroni profits into useful educational purposes, including medical education, the profits themselves were derived at the expense of taxpaying competitors of Mueller. New York University is a §501(c)(3) organization, as is respondent ACP. There is no difference between a competitive pasta company contributing its profits to New York University and ACP or the American Medical Association (AMA), for example, competing with taxpaying publishers for advertising and using the profits derived therefrom for purposes no less worthwhile than those of New York University.

The background of UBIT is well explained in *SICO Foundation* v. *United States,* 295 F.2d 924, 926 (Ct.Cl. 1961):

> As Judge Littleton pointed out in the first SICO decision, the law prior to 1951 had been rather clearly established that the destination of an organization's income was more important than the source of its income for purposes of determining exemption from taxation. Experience under this rule, however, showed it to be subject to abuse by those who would subvert its principle into a vehicle for the enjoyment of an unfair competitive advantage in the market place. . . . *The ensuing cry of "unfair competition" fell on sympathetic ears in the 81st Congress which responded with the Revenue Act of 1950.* [Emphasis supplied]

III. THE LEGISLATIVE HISTORY OF THE 1950 UBIT SHOWS THAT THE PUBLISHING BUSINESS IS SUBJECT TO UBIT AND THAT IRS HAS DISCRETION TO DETERMINE WHAT IS UNRELATED BUSINESS INCOME

Enactment of UBIT followed extensive hearings held in 1947-48 by the House Ways and Means Committee. In mentioning various types of business activities conducted by tax-exempt organizations, Chairman Knutson cited publishing *five times:*

> The types of business operations are . . . . *publishing* major newspapers and periodicals, *publishing* books in the field of scholarship and letters, *publishing* a cookbook, selling fire insurance to churches, operating barbershops, operating a dental clinic, *publishing* a magazine on amateur photography, operating jazz con-

> certs for which admissions are charged, operating a *publishing* business, carrying on research and receiving patent royalties in the following fields: (a) chemistry generally, (b) vitamin D concentrates, (c) smoke abatement, (d) paper and pulp industry. [Emphasis supplied]

Proposed Revisions of the Internal Revenue Code: Hearings Before the House Comm. on Ways and Means, 80th Cong., 1st Sess. at 1903 (1947).

The business of publishing newspapers and magazines, of course, includes advertising.

When the question arose on the floor of the House as to which unrelated business activities would be taxed and which would not, there occurred the following exchange between Congressman Dondero and Congressman Lynch:

> Mr. Dondero: With reference to the gentleman's comment that the Bureau of Internal Revenue will determine the question, will not the Bureau of Internal Revenue look to the intent of Congress as to what we intended to tax or not to tax? Perhaps it ought to be clarified in the bill because of the question [regarding taxation of Christian Brothers' wine production] the gentleman from California raised.

To which Mr. Lynch replied:

> It is not possible to define in the bill exactly every case that is going to be covered. *We have drawn it so that there is a certain amount of discretion for the determination of questions of fact as to whether or not a certain matter comes within the purview of the bill.* [Emphasis supplied]

96 Cong. Rec. 9368 (1948).

The discretion to which Congressman Lynch referred is the broad discretion accorded IRS to administer the tax laws of the United States. *United States* v. *Correll,* 389 U.S. 299, 307 (1967); *National Muffler Dealers Association* v. *United States,* 440 U.S. 472, 476-477 (1979). In doing so, IRS must therefore consider the threshold question which passage of the UBIT resolved. That question is answered in identical statements in both the House Ways and Means and Senate Finance Committee reports on the 1950 UBIT legislation as follows:

> The problem at which the tax on unrelated business income is directed is primarily that of unfair competition.

H.R. Rep. No. 2319, 81st Cong., 2d Sess. at 36 (1950); S. Rep. No. 2375, 81st Cong., 2d Sess., at 28 (1950).[7]

In summary, when Congress passed UBIT, it enacted *general* legislation which included publishing and advertising, and granted discretion to IRS to determine where and how the unrelated business tax should apply.

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[7]In July 1985 in a report entitled *Unfair Competition in the States,* the Business Coalition for Fair Competition (ABP is not a member) at p. 1 states:

> Why does this alarm us? Because too often these commercial nonprofits bring with them into the business world the special privileges they enjoy as nonprofits. These advantages – such as exemption from income, sales and property taxes and much lower postal rates – create a distinct business advantage over their for-profit, taxpaying competitors. The competition becomes inherently unfair.

IV. AFTER CONSIDERING THE VIEWPOINT OF BOTH TAXPAYING AND NON-TAXPAYING ORGANIZATIONS IRS ISSUED REGULATIONS IN 1967 WHICH MADE ADVERTISING IN ALL PERIODICALS PUBLISHED BY TAX-EXEMPT ENTITIES SUBJECT TO UBIT.

In 1960, pursuant to the authority granted to it in 1950, IRS was wrestling with how to apply UBIT to the flourishing and growing advertising businesses of tax-exempt organizations. It was this situation which led ABP to submit a memorandum to IRS questioning the tax status of such periodicals. The 1960 memorandum was later attached as Annex 10 to an ABP 1966 presentation to IRS entitled *How To Make Money in the Advertising Business Without Paying Taxes.* Both of these memoranda are included in the Congressional hearing record on the 1969 Tax Reform bill, H.R. 13270, House Ways & Means Committee, H.R. Rep. No. 91-413, 91st Cong., 1st Sess., at 1168 (1969).

The basis for the 1960 ABP memorandum was the legislative history *prior* to UBIT and the study of applicable judicial decisions and pertinent legislation concerning tax-exemption and the operation of commercial activities by tax-exempt organizations. The 1960 ABP memorandum, just as valid in 1985 as in 1960, concluded:

> Would the situation be greatly different if the tax-exempt organization were to employ a group of salesmen whose services would be available to a member for a fee? If the tax-exempt organization did employ a group of salesmen, it would obviously be promoting nothing but the individual interest of individual members, and it would come directly within the intendment of Regulation §1.501(c)(6)-1. A publication which

> carries advertising is, to all intents and purposes, a group of salesmen, and nothing more.
>
> The way by which this unwarranted and unfair competition may be eliminated should be to require the business league or the scientific organization to pay taxes on its net income received from the sale of advertising space in its publication, or in the alternative to cancel the exemption of the business league or scientific organization on the ground that its activity has exceeded that which is permissible under Section 501 of the Internal Revenue Code.

In November 1963, it was rumored that IRS would soon publish regulations applying UBIT to the advertising revenues earned by journals published by nonprofit organizations. Weithorn and Liles, *Unrelated Business Income Tax: Changes Affecting Journal Advertising Revenues,* 45 TAXES 791 (December 1967). That article stated that Commissioner Mortimer Caplin advised the Ways and Means Committee on June 26, 1964 that IRS was drafting regulations which would make an organization, otherwise exempt, subject to tax on its income from advertising in periodicals. The article said:

> However, delay followed delay (interspersed by rumors of imminent publication) as a result of (1) the strong protests unofficially expressed by numerous organizations which would be affected — generally estimated at about 700 journals with gross annual advertising revenues approximating $110 million, including, for example, *Nation's Business, Journal of the American Medical Association, National Geographic,* and (2) the Service's own technical problem of determining how to allocate journal expenses between (i) editorial

> and other textual content (clearly "related" and thus productive of nontaxable income), and (ii) advertising content (claimed to be "unrelated" and thus productive of taxable income).[8]

Finally, on April 14, 1967, IRS issued its long awaited advertising regulations. Prop. Reg. §1.513-1, 32 Fed. Reg. 5993 (1967). The storm which brewed was so great that when IRS requested comments on the proposed regulations, there were 451 responses.

IRS then held public hearings before a specially constituted panel. There were so many requests to be heard that IRS had to hire the Labor Department auditorium to accommodate all who wished to participate. One hundred and two organizations testified.

The hearing was replete with exhibits. As an example of the kind of unfair competition periodicals like *Forbes* and *Fortune,* (not members of ABP) faced, ABP showed a promotional motion picture prepared and used by the tax-exempt U.S. Chamber of Commerce, publisher of *Nation's Business,* the film entitled "The Committee of One."[9] The movie depicts the extraordinary influence the

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[8]The $110 million figure for 1963 would be a conservative $360 million in 1985, based on the 321% increase in the Consumer Price Index from 1967 to 1985. Bureau of Labor Statistics, *News,* USDL-85-252. Moreover, the number of tax-exempt organizations is now staggering: The May 13, 1985 issue of the *Non-Profit Organization Tax Letter,* cites a recent statement by IRS Commissioner Egger that there are 871,000 exempt organizations, of which 353,000 are charitable organizations and 53,000 are business leagues. (Section 501(c)(6)).

[9]In the movie, the "Committee of One" is the chairman of the board of a corporation. During the hearing, the U.S. Chamber of Commerce opposed the advertising regulations. In 1950 it supported passage of UBIT. But in 1967 the Chamber's testimony would have included advertising in *Nation's Business* as tax-exempt.

Chamber claimed it had upon the country's business leaders as a reason for buying advertising in *Nation's Business.*

On December 12, 1967, IRS and Treasury, after considering the large volume of comments received, issued the final advertising regulations in substantially the same form as had been proposed, effective for all tax years commencing after December 13, 1967. 32 Fed. Reg. 17657.

The events leading up to the issuance of the regulations were as a skirmish compared with the warfare then commenced on Capitol Hill by nonprofit organizations.

V. IN 1968 CONGRESS REJECTED LEGISLATION WHICH WOULD HAVE NULLIFED THE 1967 TREASURY REGULATIONS

The first shot was fired on the floor of the Senate March 27, 1968 when without advance notice Senator Murphy of California introduced an amendment to an excise tax bill, H.R. 15414. This amendment would have exempted advertising in the periodicals of nonprofit organizations from tax if the advertising "is substantially related to the exercise or performance by such organization of its charitable, educational or other purpose or function. . ." .[10] 114 Cong. Rec. 7879 (1968).

The Murphy amendment would have killed the Treasury advertising regulation because everything would be "related": a dentist's chair in a dental society magazine, a pharmaceutical in a medical society periodical, a convention hotel in an association executives' publication, a word processor in a bar association journal, cement in an engi-

[10]This language covered § 501(c)(3), § 501(c)(6), and other § 501(c) organizations.

neering society periodical, chemicals in a chemical society journal, *ad infinitum.*[11]

The Murphy Amendment was introduced on the floor without discussion in the Finance Committee, *Id.* at 7880. The unannounced Murphy rider passed the Senate the day it was introduced. However, when H.R. 15414 went to conference, the Murphy Amendment was deleted. Instead, House Ways and Means Committee Chairman Mills on July 1, 1968 issued Press Release No. 10 which said that his Committee would conduct public hearings within the next several weeks on the advertising regulations if its schedule permitted. As it turned out, the Committee's schedule did not permit hearings to be held before the adjournment of Congress on October 14, 1968.

But before adjournment the opponents of the Treasury advertising regulations were able to have yet another rider[12] tacked on to yet another piece of legislation – this time a soil conservation bill (H.R. 2767). This amendment (section 5 of H.R. 2767) had the ostensible purpose of postponing the effective date of the advertising regulations for one year, if not permanently postponing them.

It was at this point that more deliberative voices in the Senate took hold. Senators Anderson, Morton, Fulbright, and Metcalf announced that they would offer an amendment, No. 955, to the same soil conservation bill, to let the

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[11]Senator Murphy's amendment would have overturned the whole thrust of the source test, as contrasted with the destination test in effect prior to passage of UBIT in 1950, when Congress held that taxability would be determined not by *how* the income was used but *where it came from.*

[12]*See* S. Rep. No. 1497, 90th Cong. 2d Sess. (1968).

Treasury regulations stand until Congress held hearings on the matter in the following year.[13] 114 Cong. Rec. 26667 (1968).

In introducing that amendment on September 12, 1968 with full notice to the Senate, Senator Anderson stated:

> When the matter was before the Senate on March 27, I think we must all admit we knew very little about it. We did not know, for example, that we were opening up a loophole that could cost the general taxpayers $25 million a year, and this at a time when we are raising taxes for everyone else.

Ibid.

Senator Anderson correctly predicted:

> It is my opinion that Congress is going to reaffirm IRS when hearings are held. Certainly we did not bestow the tax-exempt privilege on organizations to become tax sanctuaries competing actively with taxpayers. If we do not reaffirm IRS, we will be giving franchise to nonprofit organizations to go into all sorts of business and we may well be killing the Unrelated Business Tax Congress passed in 1950.

Id. at 26668.

The Anderson Amendment deleting the one-year postponement was debated on the floor of the Senate September 20, 1968. 114 Cong. Rec. 27785-27788:

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[13]The Ways and Means Committee hearings were held February 21, 24-26, 1969. The Senate Finance Committee hearings were held September 11-12, 1969.

Senator Williams of Delaware declared:

> Mr. President, I support the Anderson amendment. I think it is one that should be approved. It amounts to about $25 million a year in revenues. At this particular time, I do not think the Government can afford to lose that amount of revenue. I shall support the amendment.

Id. at 27786.

Senator Pastore specified:

> First of all, I want to say that I am going to support the Senator's amendment. What I think Senators should bear in mind is that we have nothing against these groups who, in many instances, do a fine job and very good work. But we must understand that every time we alleviate, eliminate, or exempt any particular group from paying taxes, we add those taxes onto the rest of our taxpaying society. After all, a certain amount of money must be raised *and all Americans should share the burden equally: otherwise the heavier burden falls upon the remainder of American taxpayers. It is unfair to exempt them and not to exempt others.* [Emphasis supplied]

Ibid.

Senator Metcalf stated:

> . . . Existing law subjects certain tax-exempt organizations to tax on their unrelated business activities. The primary purpose of this tax is to remove the unfair competitive advantage which tax exemption would otherwise confer upon commercial activities of tax-exempt organizations. The need for application of this sound policy to the business activities of exempt organi-

> zations is nowhere clearer than it is in the area of commercial advertising appearing in exempt organization periodicals. The evidence gathered by the Treasury study and hearings graphically demonstrates that tax-exempt organizations compete against taxpaying periodicals for the sale of advertising space with all the tools available to their competitors, plus one — their exemptions.

Id. at 27787.

Senator Dirksen was the only spokesman for postponement. *Id.* at 27786.

The bipartisan Anderson Amendment passed the Senate, and the Treasury advertising regulations were saved.

VI. THE 1969 TAX REFORM ACT RATIFIED THE 1967 TREASURY REGULATIONS, THUS MAKING ALL ADVERTISING INCOME OF ALL TAX-EXEMPT ORGANIZATIONS SUBJECT TO UBIT

The hearings announced by Chairman Mills were held by the Ways and Means Committee February 21, 24-26, 1969.[14]

A. Testimony Of The Opponents Of The Regulations Demonstrates That The Opponents Including Respondent Knew Their Advertising Profits Would Be Subject To UBIT

Of the organizations testifying against the regulation, 24 were §501(c)(3) organizations like respondent ACP and 13 were §501(c)(6) organizations like AMA. All stated they would be subject to the tax.

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[14]Attached hereto as Appendix B are contemporaneous newspaper accounts by the *Washington Post* and *New York Times* of February 26, 1969 which reported the hearings.

One §501(c)(3) witness was Dr. Edward Rosenow, the Executive Director of respondent ACP. The testimony he gave before the Ways and Means Committee in 1969 is essentially the same testimony he gave in this case before Chief Judge Kozinski in the Claims Court in 1983.

Dr. Rosenow's 1969 testimony is highly relevant to the case at bar. He testified:

(1) that the Treasury Department by its regulations had usurped the power of Congress;

(2) that the new Treasury regulations had the effect of "conclusively presuming" that advertising income derived from ACP publications constituted taxable unrelated trade or business income;

(3) that the regulations set up a new test declaring that ACP's advertising was taxable even though it was related to an exempt function.

Dr. Rosenow urged Congress:

> . . . [U]ndo what the Treasury has done . . . by singling out commercial advertising, regardless of whether or not it is substantially related to the carrying out of the exempt functions . . .

The Tax Reform Act of 1969: Hearings on H.R. 13270 Before the House Comm. on Ways and Means, 91st Cong., 1st Sess. at 1113 (1969).

When Dr. Rosenow testified for respondent ACP in 1969, he stated that ACP would have to pay taxes under the Treasury advertising regulations. ACP's 1969 testimony impeaches its position in 1985 in the case at bar. After hearing Dr. Rosenow, Congress voted to give the Treasury regulations the force of law. See pp. 24-26 *infra*.

Another witness was James Low, Executive Vice President of the American Society of Association Executives, a §501(c)(6) organization. ASAE requested that a legal analysis its counsel had prepared be included in the record. *Id.* at 1184. The ASAE legal analysis described Examples 6 and 7 contained in Treasury Regulation §1.513-1(d)(4)(iv) as being "novel" and continued:

> Under the new Regulations, *all* advertising in an organization publication is now taxable (with the dubious exception of college publication advertisements). [Emphasis supplied]

Id. at 1188.

That is a correct statement.[15] Congress agreed with ASAE that all advertising is taxable. It emphasized this fact by giving the Treasury regulations the force of law. (*Infra* at 26). ASAE's 1969 legal memorandum impeaches what ASAE has said to the Court in its amicus brief opposing certiorari.

The American Chemical Society, a §501(c)(3) organization testified:

> If, in the wisdom of the Congress, it should be decided that tax-exempt scientific and educational organizations of the nature of the American Chemical Society should be taxed on their revenues, from any source, we would submit two major items. First, this determination is one for the Congress and the Congress alone, and second should such a determination be made, we are firmly convinced that it would be contrary to law to endeavor to impose such a tax in the fashion in which it has been suggested by the Internal Re-

[15]Treasury Regulation § 1.513-1(d)(4)(iv) (1967), Examples 6 and 7, Appendix A, *infra*, demonstrate this.

venue Service under the regulations to which we object.

Id. at 1128.

Congress answered the American Chemical Society by giving the Treasury regulations the force of law.

The foregoing examples are typical of all testimony delivered to Congress by those non-taxpaying organizations which opposed the advertising regulations. Some, like respondent ACP, amicus ASAE, and AMA in the United States District Court in Chicago, *supra,* still oppose them.

B. Testimony Of Taxpayers In Support Of The 1967 Treasury Regulations

There follows a brief summary of the testimony of witnesses in support of the advertising regulations.

John Babcock, President of ABP, a §501(c)(6) organization, testified:

> *It is our opinion that advertising is a business unrelated to any purpose for which any organization was granted an exemption from the income tax.* Nevertheless, tax exemption has been used by a large number of tax-exempt organizations to conduct just as competitive an advertising business as taxpaying publishers of necessity conduct in order to survive and be able to pay taxes. [Emphasis supplied]

Id. at 1145.

Mr. Babcock brought to the attention of the Committee that beneficial purposes and services are rendered not only by tax-exempt organizations, societies and foundations but by taxpayers as well. *Ibid.*

David McGrath, Senior Vice President of McGraw-Hill

Publications, compared *Chemical and Engineering News,* published by the American Chemical Society with *Chemical Week,* published by McGraw-Hill. *Id.* at 1147.

After testifying that there were over 115 identical advertisements that appeared in contemporaneous issues of both American Chemical Society's *Chemical and Engineering News* and in McGraw-Hill's competing *Chemical Week,* Mr. McGrath stated:

> Now, a question was asked earlier in this testimony about the rates. In the case of *Chemical and Engineering News* [American Chemical Society] their rates are approximately 25 percent higher than *Chemical Week* [McGraw-Hill]. Their circulation is twice as large, so their cost per 1,000 is considerably lower.
>
> If this publication was taxed it is my belief they would have to raise their advertising rates and this might make it a less attractive advertising purchase.
>
> On the other hand, if you believe McGraw-Hill ought not to pay taxes, gentlemen, we could reduce our rates which would help fight the war against inflation.
>
> It would seem logical, gentlemen, in conclusion, and, indeed, fair that in this competitive climate both magazines should have equal treatment from the tax standpoint.

Id. at 1149.

Ralph Hench, publisher of the taxpaying *American Journal of Medicine,* also testified. That publication directly competes today and directly competed in 1969 with respondent ACP's *Annals.* The current President of the company which publishes the *American Journal of*

Medicine, John K. Abely, furnished an affidavit in support of ABP's Amicus Curiae Brief in the court below, reaffirming in 1984 what Mr. Hench said in 1969. That affidavit is attached hereto as Appendix C.

The National Newspaper Association's witness was Richard Cardwell, General Counsel and Manager of the Hoosier State Press Association. He testified:

> The purpose of the so-called unrelated business income tax is really quite simple and basic. Congress determined – and we think rightly – that if tax-exempt organizations engage in business enterprises, in competition with taxpaying private-owned businesses, it would be unfair to grant the tax exempts the advantage of retaining their full profits while their private competitors pay income taxes on comparable profits.

Id. at 1105.

Congress agreed with taxpayers that advertising was a business unrelated to any tax-exempt purpose and gave the IRS regulations the force of law.

C. The Committee Reports Of Both The House And Senate Explicitly Concluded That (1) Advertising Profits Of All Tax-Exempt Organizations Are Subject To UBIT And (2) The 1967 Treasury Regulations Declaring Advertising To Be An Unrelated Trade Or Business Are Valid

After days of testimony, the House Ways and Means Committee stated as follows:

> Finally, the Internal Revenue Service promulgated regulations on December 12, 1967 which clarified the law with respect to the conduct of an unrelated trade or business carried on as a part of an exempt function. *This regulation mainly affected the advertising income of public-*

> *ations such as medical journals. There has been controversy over the validity of these regulations. Your committee wants to make clear that such regulations are valid.* [Emphasis supplied] H.R. Rep. No. 91-413, 91st Cong., 1st Sess., *reprinted in U.S. Code Cong. & Ad. News* 1965 (1967).

The Ways and Means Committee added:

> Explanation of the provision. — Because of the ensuing controversy over this problem your committee has decided to deal with this subject by legislation. In general, it is in agreement with the purpose of the regulations. Your committee believes that a business competing with taxpaying organizations should not be granted an unfair competitive advantage by operating tax free unless the business contributes importantly to the exempt function. *It has concluded that by this standard, advertising in a journal published by an exempt organization is not related to the organization's exempt functions, and therefore it believes that this income should be taxed.* [Emphasis supplied]

Id. at 1695.

The House in passing §513(c) of the Tax Reform Act of 1969 endorsed the Ways and Means Committee's findings and voted to give the Treasury advertising regulations the force of law.

The Senate Finance Committee Report accompanying §513(c) stated:

> Present law. — In December 1967, the Treasury Department promulgated regulations under which the income from advertising and similar activities is treated as *"unrelated business income" even though such advertising for example may appear*

> *in a periodical related to the educational or other exempt purpose of the organization.*
>
> General reasons for change. — The Committee agrees with the House that the regulations reached an appropriate result in specifying that *when an exempt organization carries on an advertising business in competition with other tax-paying businesses, it should pay a tax on the advertising income.* The statutory language [the 1950 Act] on which the regulations are based, however, is sufficiently unclear so that substantial litigation could result from these regulations. For this reason, *the Committee agrees with the House that the regulations, insofar as they apply to advertising and related activities, should be placed in the tax laws.* [Emphasis supplied]

S. Rep. No. 91-552, 91st Cong., 1st Sess., *reprinted in U.S. Code Cong. & Ad. News* 2104 (1969).

Under the heading "Income from advertising, etc., activities (sec. 513 of the Code)," the final conference committee report follows the House report. S. Doc. No. 91-782, 91st Cong., 1st Sess., *reprinted in U.S. Code Cong. & Ad. News* 2406 (1969).

VII. CONGRESS' CLEAR INTENT IN 1969 TO APPLY UBIT TO ALL ADVERTISING WAS FRUSTRATED BY THE ERRONEOUS FEDERAL CIRCUIT DECISION

As this Court has said: "Where Congressional intent is discernible — and here it seems crystal clear — we must give effect to that intent." *Sinclair Refining Co.* v. *Atkinson,* 370 U.S. 195, 215 (1962).

With crystal clear legislative history supporting the Treasury regulations in 1969, 1978 (*supra* at 6), and 1981

through 1984 (*supra* at 6), and with witnesses opposed to the regulations actually stating that they knew they would be taxed if Congress passed §513(c), and with Congress having rejected every attempt to reopen this subject, it is incredible that the Federal Circuit would usurp the taxing power of Congress and in the instant case overturn the trial court.

What IRS did when it published its advertising regulations in 1967 was to establish a rule declaring advertising of tax-exempt organizations like respondent American College of Physicians taxable *per se.* What Congress did in 1969 was (1) declare the IRS advertising regulations valid, H.R. Rep. No. 91-413, 91st Cong., 1st Sess., *reprinted in U.S. Code Cong. & Ad. News* 1695 (1969); (2) declare advertising unrelated to any tax-exempt purpose, *Id.* at 1696; (3) single out the advertising income of medical journals as taxable, *Id.* at 1690; and (4) declare that the regulations should be placed in the tax laws. S. Rep. No. 91-552, 91st Cong., 1st Sess., *reprinted in U.S. Code Cong. & Ad. News* 2104 (1969).

Valid Treasury regulations like Example 7, *supra,* applicable to respondent ACP, should not be disregarded by the courts as happened in the Federal Circuit![16] This Court held in *United States* v. *Correll, supra* at 307, as follows:

> Congress has delegated to the Commissioner, not to the courts, the task of prescribing "all needful rules and regulations for the enforcement" of the

[16]Even respondent has not challenged Example 7. Its brief opposing certiorari in this case states (p.12):

> While it is true that the Court of Appeals did not discuss the validity *vel non* of Example 7, this silence is perfectly understandable because the College never challenged Example 7.

> Internal Revenue Code. 26 U.S.C. §7805(a). In this area of limitless factual variations, "it is the province of Congress and the Commissioner, not the courts, to make the appropriate adjustments." Commissioner v Stidger, 386 U.S. 287, 296, 18 L.ed.2d 53, 59, 87 S. Ct. 1065. The role of the judiciary in cases of this sort begins and ends with assuring that the Commissioner's regulations fall within his authority to implement the congressional mandate in some reasonable manner. Because the rule challenged here has not been shown deficient on that score, the Court of Appeals should have sustained its validity.

The vivid and protracted administrative and legislative history delineated herein overwhelmingly proves how far the United States Court of Appeals for the Federal Circuit strayed in this case when it judicially preempted the will of Congress.

Of great consequence will be the inevitable erosion of UBIT itself which will follow if the decision of the Federal Circuit is allowed to stand. If anything, fair competition and the tax revenues of the United States require reinforcement of UBIT to prevent debilitation. That is why ABP's amicus curiae brief supporting the Government petition for certiorari states:

> If ever a case cried out for appellate correction of judicial error, this is that case.

CONCLUSION

WHEREFORE, ABP respectfully requests this Court to reverse the United States Court of Appeals for the Federal Circuit.

Respectfully submitted,

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Joseph J. Saunders

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September 1985

APPENDIX A

§ 1.513-1(d)(4)(iv)
(iv) Exploitation of exempt functions.

(iv) Exploitation of exempt functions. In certain cases, activities carried on by an organization in the performance of exempt functions may generate good will or other intangibles which are capable of being exploited in commercial endeavors. Where an organization exploits such an intangible in commercial activities, the mere fact that the resultant income depends in part upon an exempt function of the organization does not make it gross income from related trade or business. In such cases, unless the commercial activities themselves contribute importantly to the accomplishment of an exempt purpose, the income which they produce is gross income from the conduct of unrelated trade or business. The application of this subdivision is illustrated in the following examples:

* * * * *

Example (6). Z is an association exempt under section 501(c)(6), formed to advance the interests of a particular profession and drawing its membership from the members of that profession. Z publishes a monthly journal containing articles and other editorial material which contribute importantly to the accomplishment of purposes for which exemption is granted the organization. Income from the sale of subscriptions to members and others in accordance with the organization's exempt purposes, therefore, does not constitute gross income from unrelated trade or business. In connection with the publication of the journal, Z also derives income from the regular sale of space and services for general consumer advertising, including advertising of such products as soft drinks, automobiles, articles

of apparel, and home appliances. Neither the publication of such advertisements nor the performance of services for such commercial advertisers contributes importantly to the accomplishment of any purpose for which exemption is granted. Therefore, notwithstanding the fact that the production of income from advertising utilizes the circulation developed and maintained in performance of exempt functions, such income is gross income from unrelated trade or business.

Example (7). The facts are as described in the preceding example, except that the advertising in Z's journal promotes only products which are within the general area of professional interest of its members. Following a practice common among taxable magazines which publish advertising, Z requires its advertising to comply with certain general standards of taste, fairness, and accuracy; but within those limits the form, content, and manner of presentation of the advertising messages are governed by the basic objective of the advertisers to promote the sale of the advertised products. While the advertisements contain certain information, the informational function of the advertising is incidental to the controlling aim of stimulating demand for the advertised products and differs in no essential respect from the informational function of any commercial advertising. Like taxable publishers of advertising, Z accepts advertising only from those who are willing to pay its prescribed rates. Although continuing education of its members in matters pertaining to their profession is one of the purposes for which Z is granted exemption, the publication of advertising designed and selected in the manner of ordinary commercial advertising is not an educational activity of the kind contemplated by the exemption statute; it differs fundamen-

tally from such an activity both in its governing objective and in its method. Accordingly, Z's publication of advertising does not contribute importantly to the accomplishment of its exempt purposes; and the income which it derives from advertising constitutes gross income from unrelated trade or business.

APPENDIX B

WASHINGTON POST FEBRUARY 26, 1969

Exempt Status Provokes Tax Hearing Battle

By Frank C. Porter
Washington Post Staff Writer

The battle over whether advertising income from publications of tax-exempt organizations should be taxed flared anew yesterday as the House Ways and Means Committee continued its hearings on tax reform.

The controversy finds leading commercial trade and professional publications such as Business Week, the American Journal of Medicine and Chemical Week ranged against their non-profit counterparts—Nation's Business, published by the Chamber of Commerce of the United States; the Journal of the American Medical Society, and Chemical & Engineering News, official organ of the American Chemical Society.

Also involved are such historic household standbys as the National Geographic and Boys' Life, a publication of the Boy Scouts of America—both non-profit ventures.

Anticipates Argument

The American free enterprise system cannot exist, said John B. Babcock, president of American Business Press, Inc., "if we have one business paying an income tax on its profits and a competitor paying no income tax on its profits."

But "to say these magazines compete in the market place is a misrepresentation," James P. Low, executive vice president of the American Society of Association Executives, told the Committee.

Babcock had already anticipated this argument, however, by having the spacious hearing room darkened and screening a hard-sell promotion film used by Nation's Business. The film wooed potential advertisers with self-assured claims that their message would reach far more of the Nation's business decision-makers in Nation's Business than in Business Week or Fortune.

Babcock's organization represents McGraw-Hill, publisher of Business Week, as well as other large trade publication chains.

Tried for Amendment

Under law tax-exempt organizations are required to

pay taxes on "unrelated" business income. Until late 1967 advertising revenues from such periodicals as Nation's Business and the National Geographic were considered "related" and consequently escaped taxation.

But then the Internal Revenue Service ruled that such income was indeed "unrelated" and the non-profit publications have had to pay taxes, not on their total income, but on advertising revenues.

The tax-exempt groups tried in vain last summer to push through an amendment to the Revenue Act of 1968 that would have overturned the IRS ruling.

Now Ways and Means has placed the question on its agenda for comprehensive reform of the Nation's entire tax system.

Ruling Called 'Capricious'

Babcock and others yesterday argued that advertising in itself is unrelated to the purposes of such groups as the AMA, Boy Scouts and Chamber of Commerce.

Their opponents claimed the IRS ruling was capricious, overrode the intent of Congress and was inconsistent in splitting an integrated operation into taxable advertising and an untaxed editorial operation.

They further argued that the content of their advertising is indeed related to their exempt purposes and that the advertising revenues, undiluted by taxes, are necessary to carry on their main activities—scouting, for example.

Babcock said that a number of members of the American Business Press, which represents some 500 organizations, have resigned from the Chamber of Commerce in protest against its position of "opposing for itself the free enterprise principles it espouses for others."

NEW YORK TIMES FEBRUARY 26, 1969

Tax-Exempt Groups Score U.S. Ruling

WASHINGTON, Feb. 25 (UPI) —The House Ways and Means Committee was asked today to help overturn an Internal Revenue Service ruling that tax-exempt organizations must pay taxes on income from advertisements in their publications.

James P. Low, representing 2,900 professional tax-exempt associations that publish trade magazines, said that the income, which yielded "little net revenue," was essential to cover costs of publication as a service to subscribers.

But representatives of commercial magazine publishers defended the ruling and criticized such groups as the American Medical Association and the Chamber of Commerce of the United States for failing to practice what they preached about free enterprise.

Rree enterprise, said John B. Babcock, "cannot exist if we have one business paying an income tax on its profits and a competitor paying no income tax on its profits."

Mr. Babcock is president of the American Business Press, Inc., representing 500 commercial business publications. He said that some of his member publishers had quit the Chamber of Commerce "because of the position it has taken in opposing for itself the free enterprise principles it espouses for others."

Ruling Outlined

The Revenue Service ruled in December, 1967, that advertising income from publications of tax-exempt organizations was "unrelated" to the educational, scientific or charitable purposes for which the tax immunity was granted and therefore must be taxed.

An effort to overturn the ruling failed in Congress last year. The committee is now investigating possible abuses of tax laws.

Mr. Babcock showed the committee a film produced by the Chamber encouraging advertising in its magazine, Nation's Business. He said that tax-exempt groups competed just as vigorously for advertising as commercial, taxpaying publishers, who must do so to survive.

Ralph W. Hench Jr., representing publishers of commercial magazines, said that the medical association, with a net worth of more than $19-million in 1967, paid advertising agencies $2.2-million in commissions in 1966 for business placed in its journals.

APPENDIX C

AFFIDAVIT OF JOHN K. ABELY IN SUPPORT OF MOTION OF AMERICAN BUSINESS PRESS FOR LEAVE TO FILE BRIEF AMICUS CURIAE IN SUPPORT OF SUGGESTION OF UNITED STATES FOR REHEARING EN BANC

IN THE UNITED STATES COURT OF APPEALS
FOR THE FEDERAL CIRCUIT

APPEAL NO. 84-715

THE AMERICAN COLLEGE OF PHYSICIANS
Appellant

v.

THE UNITED STATES
Appellee

STATE OF NEW YORK)
) SS
COUNTY OF NEW YORK)

I, John K. Abely, being duly sworn, depose and say:

1. That I am President of Technical Publishing Co., an independent division of the Dun and Bradstreet Corporation. I have been professionally engaged in publishing for 27 years.

2. Technical publishes 21 medical, technical and business periodicals. These include the *American Journal*

of Cardiology, the *American Journal of Medicine*, the *American Journal of Surgery* and *Cutis* (a journal publishing clinical articles in dermatology), which comprise the Yorke Medical Group of Technical Publishing. All of our publications are published for-profit and are tax-paying journals.

3. Other periodicals published by Technical include *Dun's Business Monthly*, *Datamation*, *Plant Engineering* and *Solid State Technology And Research and Development*.

4. I have read the decision of the United States Court of Appeals for the Federal Circuit in *American College of Physicians* v. *United States*, slip op. no. 84-715. I am shocked by the conclusion in the Court's Opinion that the commercial advertising in the *Annals of Internal Medicine* should be tax-exempt. This decision, in my opinion, gives publishers of non-profit journals, which compete with tax-paying periodicals, a green light to again engage in unfair competition with us and other publishers.

5. At Technical, and I know I reflect the view of the 500 specialized tax-paying periodicals which belong to the American Business Press, we thought the issue of the unrelated business tax had been put to rest in 1969 when Congress specifically applied the unrelated business tax to advertising. Now to my amazement, the Court has said our competitors do not have to pay taxes on their advertising profits, because the advertising in *Annals* is allegedly related to the tax-exempt function of the owners of *Annals*. (slip op. at 18).

The same type of advertising appearing in *Annals* appears in our *American Journal of Medicine* and other medical periodicals. Each of our four medical journals

limits the type of advertising in the same manner as *Annals*. Each of our journals has a distinguished board of doctors who provide peer review as does *Annals*. From time to time, the same doctors who provide peer review for *Annals*, perform the same function for our medical journals.

The advertisements carried both in *Annals* and our journals do not announce new developments alone, but are printed month after month, as is the case with most commercial advertising, in order to make it effective.

Advertisements are aggressively solicited by salesmen representing the American College of Physicians. These solicitations are made to pharmaceutical manufacturers and to their advertising agencies. Out on the street the battle is for a share of an advertiser's budget: there may not be enough to place the same advertisement in both *Annals* and one of our journals. Advertisements published in *Annals* are sold at competitive rates in *Annals* and in our journals: the difference is that if this decision is upheld, *Annals* will not have to pay taxes on its advertising profits, but we will. This is unfair competition.

6. On February 25, 1969, when Congress held hearings on the unrelated business tax, Congress was particularly concerned with application of the tax to advertising in nonprofit journals like *Annals*. Ralph Hench, then President of our medical publications, testified before the House Ways and Means Committee in support of the IRS regulations of 1967 which applied the unrelated business tax to advertising profits of nonprofit journals like *Annals*. He emphasized the unfair competition that his competitors like the *AMA Journal* and *Annals* were able to mount against him by virtue of their tax exemption.

7. I note that Dr. Edward Rosenow, Executive Director of *Annals*, appeared in the same hearing as Mr. Hench. And I further note that Congress ruled as Mr. Hench and others thought and not as Appellant and other would-be tax avoiders urged.

Nothing has happened in the last 15 years in the world of medical publishing to make the testimony of Mr. Hench any less relevant: if anything, there has been a proliferation of medical journals – some nonprofit, some for-profit. All of them are fiercely battling in a competitive marketplace for the medical advertising dollar. There should be no unfair tax advantage to any.

8. The reason why pharmaceutical companies advertise in medical journals is because they want to sell their products to readers who are in a position to buy their products. This is true of *Annals,* of our own journals and of all other journals that carry advertising. Let's face it: The purpose of advertising is to sell products. If *Annals* does not agree with this, it has a clear option: Let it provide its advertising without charge. Then there would be no income and therefore no tax.

9. I attach as Attachment 1 an advertisement *Annals* bought and paid for in *Medical Advertising News.* The purpose of this advertisement is to solicit additional advertising for *Annals.* Appropriately, *Annals'* advertisement is entitled "The Bottom Line," a financial term, not a term usually associated with nonprofit organizations. The advertisement gives both the names and telephone numbers of *Annals'* "sales representatives." It strikes me as anomalous that an organization exempt from Federal taxation has "sales representatives."

10. *Annals* has a sister tabloid publication published by the same nonprofit organization. Its title is *"The*

Observer." *Annals* conducts a joint advertising campaign with *The Observer.* Attachment 2 is an advertisement urging advertisers to advertise in both periodicals. I note that the advertisement states "Plan on scheduling *ACP Observer* and *Annals* to cash in on the clout of the Stellar Journal/Tabloid Team." The emphasis is on "cash[ing] in." How is "cashing in on the clout" of any tax-exempt organization related to any tax-exempt purpose?

11. Back issues of *Annals,* upon request, are bound into volumes. When so bound, the advertising pages are deleted because, according to *Annals,* these pages are "extraneous material." (*Annals,* March 1983, p. I-117). That *Annals* follows this practice is further proof that the true purpose of *Annals'* advertising is to make money for the doctors who make up the ownership of the periodical.

12. If the three-judge panel's decision in this proceeding is upheld, its effects will be widespread, going far beyond the medical publishing field. All types of nonprofit journals will claim their advertising is "substantially related" to their tax-exempt purpose. We heard all these arguments in 1969 when we testified before Congress. Congress turned those arguments down, but unfortunately, the three-judge panel now has opened up a loophole for tax-exempt advertising and unfair competition. Trade associations, universities, professional societies and others which publish journals will even more aggressively market their journals to advertisers to take competitive advantage of the Court's Opinion.

In the meantime, journals like our *American Journal of Medicine* which pays taxes, will have to compete for the same advertising dollars as the *Annals of Internal Medicine.*

/s/ John K. Abely
John K. Abely

Sworn and subscribed before me this 29 day of October, 1984.

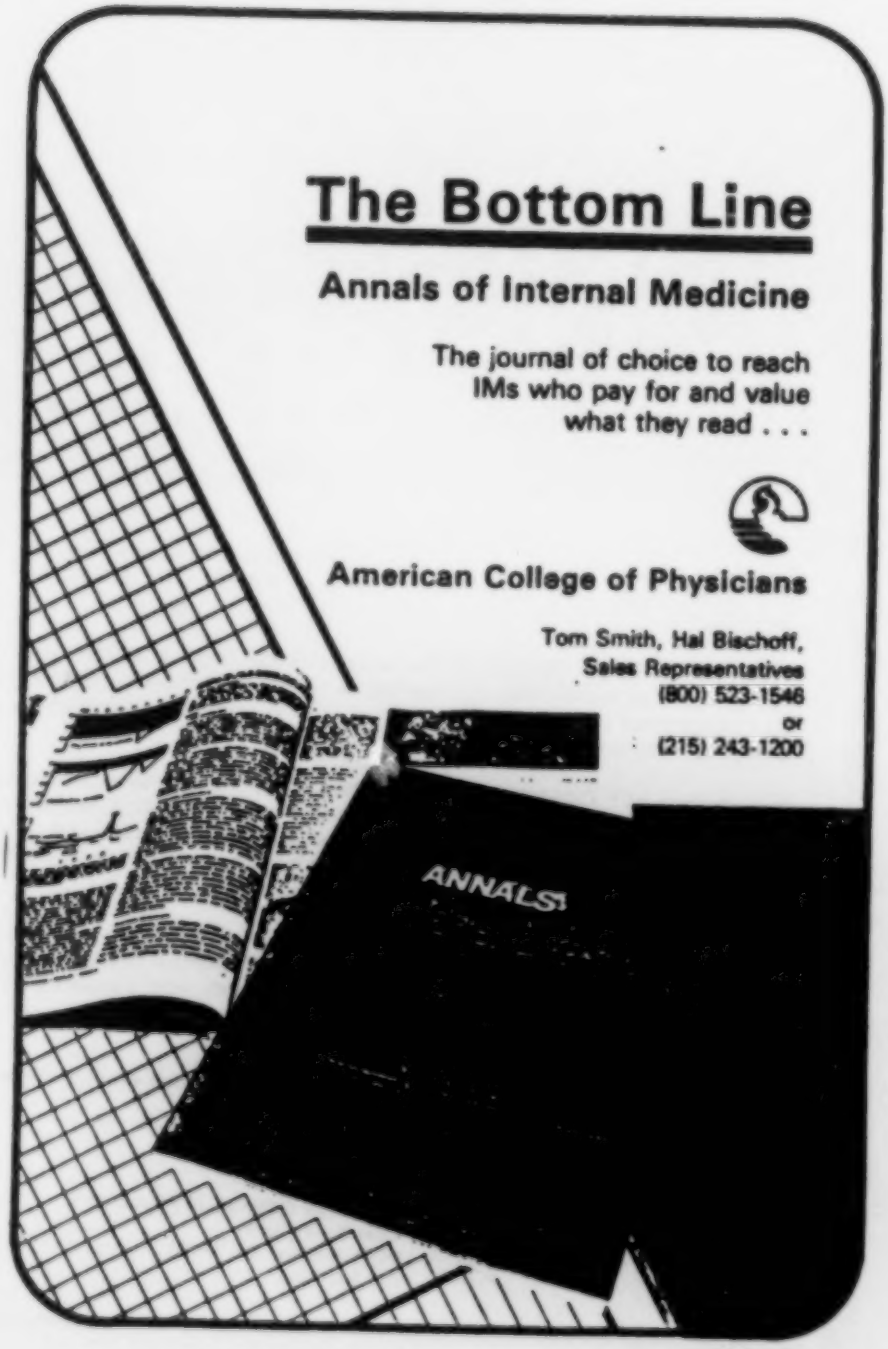
My commission expires

STATE OF NEW YORK
NEW YORK COUNTY

JOSEPH J. ZACCARIA, Notary Public
State of New York, 31-437550
Qualified in New York County
Commission Expires March 30, 1985

/s/ Joseph J. Zaccaria
Notary Public

Attachment No. 1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Attachment No. 2

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